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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

THOMAS FERNANDEZ, LORA SMITH,
and TOSHA THOMAS

Plaintiffs,

vs.

K-M INDUSTRIES HOLDING CO., INC.;
K-M INDUSTRIES HOLDING CO., INC.
ESOP PLAN COMMITTEE; WILLIAM
E. AND DESIREE B. MOORE
REVOCABLE TRUST; TRUSTEES OF
THE WILLIAM E. AND DESIREE B.
MOORE REVOCABLE TRUST; CIG
ESOP PLAN COMMITTEE; NORTH
STAR TRUST COMPANY; DESIREE B.
MOORE REVOCABLE TRUST;
WILLIAM E. MOORE MARITAL
TRUST; WILLIAM E. MOORE
GENERATION-SKIPPING TRUST; and
DESIREE MOORE, BOTH IN HER
INDIVIDUAL CAPACITY AND AS
TRUSTEE OF THE WILLIAM E AND
DESIREE B. MOORE REVOCABLE
TRUST'S SUCCESSOR TRUSTS
NAMED ABOVE,

Defendants.

Case No. C06-07339 CW

**NORTH STAR TRUST COMPANY'S
REPLY MEMORANDUM IN SUPPORT
OF ITS MOTION FOR LEAVE TO FILE
MOTION FOR RECONSIDERATION OR,
ALTERNATIVELY, FOR ENTRY OF
JUDGMENT**

1 **I. INTRODUCTION**

2 Section 2(b) of the Stock Purchase Agreements that established the ESOP obligates the
3 Moore Trust to reimburse the ESOP, upon a determination by a court that the ESOP overpaid the
4 Moore Trust for the stock the ESOP holds, for the amount of that overpayment plus interest. For
5 Plaintiffs to succeed in their case against North Star Trust Company (“NSTC”), this Court must
6 find that the ESOP overpaid the Moore Trust for the stock the ESOP holds; Plaintiffs in their
7 opposition do not contend otherwise. NSTC seeks leave to file a motion for reconsideration of
8 the Court’s August 21, 2009 Order because the Court’s ruling that section 2(b) is an
9 “indemnification” of NSTC by the Moore Trust in violation of ERISA, amounts to a manifest
10 failure by the Court to consider the plain contractual obligations of the Moore Trust to the ESOP
11 contained in the Stock Purchase Agreements. Section 2(b) is not an indemnification of NSTC,
12 and it does not relieve NSTC of any liability for alleged breaches of fiduciary duties. Rather, it is
13 a separate contractual obligation of the Moore Trust that will be triggered the moment (if ever)
14 that the Court finds that the ESOP overpaid for the K-M stock, as the Court must find for the
15 Plaintiffs to be successful in their litigation against NSTC. Plaintiffs provide no authority, or
16 logical explanation, why the Court should not enforce section 2(b) of the Stock Purchase
17 Agreements.

18 Should the Court decide not to permit NSTC to file a motion for reconsideration of the
19 ruling on the enforceability of Section 2(b), the Court should nevertheless certify the judgment as
20 final under Rule 54(b). The Settling Defendants, who previously requested certification but now
21 reverse their position for what can only be tactical reasons, provide no convincing reason not to
22 certify. They rely upon out of circuit authority and ignore applicable Ninth Circuit guidance.
23 They identify no issue that would be presented on an immediate appeal and would be
24 readjudicated before this Court and presented again in a later appeal. They assert no reason at all
25 why a delayed appeal would be just. The Court should certify as final the judgment as to the
26 Settling Defendants.

1 **II. THE COURT SHOULD GRANT NSTC LEAVE TO FILE A MOTION FOR**
 2 **RECONSIDERATION**

3 **A. Leave to File a Motion to Reconsider Should Not be Denied Based on**
 4 **Noncompliance with Local Rule 7-9**

5 The Settling Parties argue that the Court should deny leave to file a motion to reconsider
 6 because, they say, NSTC has flouted Local Rule 7-9, which sets forth the pertinent procedure.
 7 This argument should be rejected.

8 First, the Settling Parties assert that NSTC violated Local Rule 7-9 because it filed a
 9 motion for reconsideration concurrently with its Motion for Leave to File a Motion for
 10 Reconsideration. Settling Parties' Opposition to Motion for Leave to File Motion for
 11 Reconsideration and Entry of Judgment [Dkt. # 337] ("Opp.") at 2:11-25. This assertion is
 12 manifestly false. NSTC's motion for leave is clearly styled as such; and in its memorandum in
 13 support of its motion for leave, NSTC briefly set forth the reasons it believes the Court should
 14 grant NSTC the opportunity to brief fully a motion for reconsideration. NSTC did not
 15 concurrently file any separate motion for reconsideration. Indeed, the Settling Parties' argument
 16 stands Local Rule 7-9 on its head, because their logic is that no party seeking leave to file a
 17 motion to reconsider should be permitted to explain why.

18 Second, the Settling Parties assert that NSTC offended Local Rule 7-9 by repeating
 19 argument. Opp. at 2:26-3:14. This assertion too ignores the language of the Rule, which
 20 provides that leave for a motion for reconsideration may be granted upon a "specific[] show[ing]"
 21 of "[a] manifest failure by the Court to consider material facts or dispositive legal arguments
 22 which were presented to the Court." Local Rule 7-9(b)(3). Obviously, NSTC can make the
 23 requisite showing only by demonstrating that the Court failed to consider material facts or
 24 dispositive arguments that were previously presented. The showing that the Rule itself requires
 25 cannot be rejected as "repetition."

26 **B. The Settling Parties Do Not Deny That Section 2(b) Would Be Triggered by A**
 27 **Finding That NSTC Breached Its Fiduciary Duty**

28 Plaintiffs allege in this case that NSTC breached its fiduciary duties in 2003 by failing to

1 take action to recover from the Moore Trust the overpayments that Plaintiffs allege the Moore
 2 Trust received from the ESOP in 1998 and 1999. As Plaintiffs also allege, such overpayments
 3 would have been prohibited transactions, and breaches of fiduciary duty, by the ESOP's then
 4 trustee. It appears to be undisputed that a determination by the Court that the ESOP overpaid the
 5 Moore Trust in 1998 and/or 1999 would trigger the contractual promise made by the Moore Trust
 6 in section 2(b),¹ to transfer to the ESOP the overpaid amount, with interest.

7 The Settling Parties attempt to distract the Court from this contract analysis of the Stock
 8 Purchase Agreements by framing NSTC's counterclaim to enforce section 2(b) as one for
 9 indemnification. The Settling Parties argue that "[t]he fact that the Moore Trust's liability would
 10 be triggered only if [NSTC] is found liable demonstrates that such a claim is for indemnification"
 11 and that any claim to the contrary is "merely a game of semantics." Opp. at 5:10-19. Settling
 12 Parties' argument is flawed for several reasons.

13 First, it is simply not true that "the Moore Trust's liability would be triggered only if
 14 [NSTC] is found liable" – the converse is true. For example, the Court could find that NSTC was
 15 not imprudent and did not breach its fiduciary duties (*e.g.*, because it followed a prudent process
 16 in its 2003 investigation) but that the Moore Trust did in fact receive more than adequate
 17 consideration from the ESOP. If the Court were to conclude that the Moore Trust did receive
 18 more than adequate consideration, section 2(b) would require the Moore Trust to repay the ESOP
 19 *whether or not NSTC breached its duties*. On the other hand, a finding that the ESOP did not
 20 overpay would mean that NSTC's conduct did not cause a loss to the ESOP. *See Fernandez v. K-*

21 ¹ Section 2(b) of the Stock Purchase Agreements provides, in pertinent part:

22 "In the event that there is a final determination by the Internal Revenue Service, a court of
 23 competent jurisdiction or otherwise that the fair market value of the Shares as of this date is less
 24 than the Purchase Price paid by the Trustee, then Selling Shareholder [the Moore Trust] shall
 25 transfer to the Trustee an amount . . . equal in value to the difference between the Purchase Price
 26 and said fair market value for all such Shares. . . . [S]uch shares shall be valued at their fair
 27 market value as of the date hereof and interest at a reasonable rate from the date hereof to the date
 28 of payment shall be paid by Selling Shareholder on the amount of cash paid."

This provision is triggered by any "determination" that the ESOP overpaid – whether made by a
 court, the IRS, the DOL, a successor trustee, or otherwise -- but NSTC could not enforce the
 provision absent such a determination. Where the provision is triggered, the trustee is a conduit
 for the return to the ESOP of the overpayment (plus interest).

1 *M Indus. Holding Co.*, 585 F. Supp. 2d 1177, 1184 (N.D. Cal. 2008) (finding that NSTC’s
 2 potential liability is dependent upon “the alleged breaches of fiduciary duty that took place before
 3 it was appointed the ESOP trustee”). Regardless of whether NSTC’s alleged breach is, as the
 4 Settling Parties state, “independently actionable,” the Settling Parties have not identified any way
 5 in which NSTC’s conduct harmed, or could have harmed, the ESOP unless the Moore Trust
 6 received more than adequate consideration thus triggering section 2(b).

7 Second, the Settling Parties’ argument fails because it is based on the false assertion that
 8 section 2(b) is an indemnity clause. The Settling Parties conclude that because this Court has
 9 rejected any claim by NSTC for indemnification against the Moore Trust Defendants, then the
 10 Court must also reject the enforcement of section 2(b) against the Moore Trust. Opp. at 4:15-
 11 5:20. But, as NSTC stated in its request for leave, section 2(b) manifestly is not an indemnity
 12 clause; it does not use the word “indemnity,” and NSTC does not contend that section 2(b) is an
 13 indemnity² or that section 2(b) requires the Moore Trust to reimburse NSTC for losses caused by
 14 NSTC’s actions – the definition of an indemnity. “Indemnify” means “to reimburse (another) for
 15 a loss suffered because of a third party’s . . . act or default.” BLACK’S LAW DICTIONARY (8th ed.
 16 2004). Section 2(b) does not create an indemnity. Section 2(b) will not reimburse the ESOP for a
 17 loss suffered because of NSTC’s actions; instead, section 2(b) creates an enforceable contractual
 18 obligation between the Moore Trust and the ESOP for a loss caused by the actions of the Moore
 19 Trust and the original trustee in 1998 and 1999. It is the Settling Parties who base their argument
 20 on semantics by calling section 2(b) an indemnification.

21 Indeed, the Settling Parties admit as much. They concede that NSTC’s claim “under 2(b)

22 ² The Settling Parties attempt to mischaracterize NSTC’s prior arguments on the cross-motions
 23 for judgment as explicitly claiming that section 2(b) created rights to indemnity from the Moore
 24 Trust Defendants. Opp. at 4:17-21. A careful read of NSTC’s opening memorandum in support
 25 of its motion for judgment reveals that NSTC referenced only section 7 of the Stock Purchase
 26 Agreements as a “broad indemnification provision” and cited section 2(b) as merely one of the
 Moore Trust’s covenants under those same agreements. See Dkt. #274 at 7. In the reply brief in
 support of its motion for judgment, NSTC clearly referred to section 2(b) as a provision “to make
 the Plan whole for any overpayment” in the Stock Purchase transactions. Dkt. # 307 at 16.

27 Section 7 is manifestly different from section 2(b). In section 7, the Moore Trust and the trustee
 28 agreed to cross-indemnify each other. Section 2(b) is not an indemnity provision and obligates
 only the Moore Trust.

would not have been one for indemnification, but instead would have been a claim asserted on behalf of participants to enforce the contract by its plain terms” had it been brought earlier. Opp. at 4:7-9. The Settling Parties provide no authority, or even explanation, for why the timing of the interpretation and enforcement of section 2(b) converts it into an indemnity clause.³ As noted above, section 2(b) cannot be enforced until a determination of an overpayment is made.

C. ERISA Does Not Prohibit Enforcement of Section 2(b)

The Settling Parties argue, without citation to any authority, that the Court should not require the Moore Trust to satisfy its obligation to the ESOP should the Court determine the ESOP overpaid for its stock because NSTC should not benefit from the operation of section 2(b). This argument fails for three reasons. First, as noted in the preceding paragraph, the Settling Parties concede that section 2(b) was and is enforceable – they are simply playing a word-game with the timing of section 2(b)’s enforceability. Second, the Settling Parties offer no legal support for the proposition that a contract is unenforceable merely because it may benefit a third party, such as NSTC. Third, even if there were a benefit to NSTC from the operation of section 2(b) (which NSTC disputes) by the Court enforcing the Moore Trust’s obligation to pay to the ESOP any overpayment the Moore Trust received, it is an incidental benefit. The Settling Parties do not dispute that ERISA permits a fiduciary to receive an incidental benefit from an action that benefits an ERISA plan. *See Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432, 445-46 (9th Cir. 1999) (fiduciary does not breach its duty if it is incidentally benefited by administration of pension plan); *Morse v. Stanley*, 732 F.2d 1139 (2d Cir. 1984) (it is not a fiduciary violation to take a course of action that promotes interests of plan participants simply because it incidentally benefits a fiduciary). If the ESOP is made whole through the operation of section 2(b), then Plaintiffs’ claim against NSTC, a claim that triggers section 2(b), is rendered moot as to the harm that Plaintiffs allege was caused to the ESOP. The Court’s enforcement of a contractual

³ To the extent that the Settling Parties argue that this Court’s final approval of the partial class action settlement alters the enforceability of section 2(b), this argument directly conflicts with the Court’s unqualified holding, subsequent to the final order approving the class action settlement, that Section 2(b) “requires the Moore Trust Defendants to return to the ESOP any amounts they are found to have wrongfully received as a result of the plan’s overpayment.” Order [Dkt. # 330] at 15-16.

1 provision for the benefit of the ESOP cannot be deemed an improper benefit to NSTC.

2 **D. Enforcement of Section 2(b) Will, as a Practical Matter, End the Litigation**

3 Finally, the Settling Parties assert that enforcing section 2(b) will not end this litigation
4 because Plaintiffs will “still have the right to a liability determination, equitable and injunctive
5 relief, and an award of attorneys’ fees against [NSTC]” as well as the right to pursue legal fees
6 that KMH has already advanced. Opp. at 6:2-10. This assertion is erroneous. As discussed
7 above, the Plaintiffs’ right to a liability determination would be moot as to damages because
8 Plaintiffs would recover the ESOP’s losses plus interest under section 2(b). Because NSTC is no
9 longer trustee, any demand for equitable or injunctive relief is likewise moot. And any claim for
10 attorneys’ fees or reimbursement of fees already advanced is ancillary to the merits.

11 **III. IN THE ALTERNATIVE, THE COURT SHOULD ENTER JUDGMENT FOR**
12 **THE SETTling DEFENDANTS BECAUSE THE CLAIMS AGAINST THEM**
13 **HAVE BEEN FINALLY RESOLVED AND THERE IS NO JUST REASON FOR**
14 **DELAY**

15 In considering whether entry of judgment is appropriate under Rule 54(b), the Ninth
16 Circuit takes a “pragmatic approach focusing on severability and efficient judicial
17 administration.” *Continental Airlines, Inc. v. Goodyear Tire & Rubber Co.*, 819 F.2d 1519, 1525
18 (9th Cir. 1987). “The Rule 54(b) claims do not have to be separate from and independent of the
19 remaining claims.” *Texaco, Inc. v. Ponsoldt*, 939 F.2d 794, 797 (9th Cir. 1991), *quoting Sheehan*
20 *v. Atlanta Int’l Ins. Co.* 812 F.2d 465, 468 (9th Cir. 1987); *Alcan Aluminum Corp. v. Carlsberg*
21 *Fin. Corp.*, 689 F.2d 815, 817 (9th Cir. 1982). Entry of final judgment for a party under Rule
22 54(b) is proper if all of the claims against that party have been finally adjudicated, or if the nature
23 of the claims already determined is such that an appellate court would not have to decide the same
24 issue more than once even if there were subsequent appeals. *Continental Airlines, Inc.*, 819 F.2d
25 at 1525; *Alcan Aluminum Corp.*, 689 F.2d at 817; *O2 Micro Int’l Ltd. v. Monolithic Power Sys.,*
26 *Inc.*, Case No. C 04-2000 CW, C 06-2929 CW, 2007 WL 2070275 (N.D. Cal. July 16, 2007).⁴

27 ⁴ Indeed, the Ninth Circuit has stated that the case upon which Plaintiffs chiefly rely, *Morrison-*
28 *Knudsen Co. v. Archer*, 655 F.2d 962 (9th Cir. 1981), contains an “outdated and overly restrictive
view of the appropriateness of Rule 54(b) certification.” *Texaco, Inc.*, 939 F.2d at 798.

1 The Settling Parties urge that the Court must consider a specific list of factors in deciding
 2 whether entry of judgment under Rule 54(b) is appropriate. Opp. at 9:3-13, *citing General*
 3 *Acquisition, Inc. v. GenCorp, Inc.*, 23 F.3d 1022, 1030 (6th Cir. 1994). This argument misses the
 4 mark because it relies on a Sixth Circuit case that the Settling Parties incorrectly identify as a
 5 Ninth Circuit case. Opp. at 9:10. As noted above, the Ninth Circuit does not apply the Sixth
 6 Circuit's test. Moreover, the Sixth Circuit describes its list of factors as "non-exhaustive."
 7 *General Acquisition, Inc.*, 23 F.3d at 1030.

8 **A. The Legal Issues Remaining in the Case Are Distinct From Those Asserted**
 9 **Against and Decided in Favor of the Settling Defendants, Such That The**
 10 **Ninth Circuit Would Not Have To Consider The Same Issues More than Once**

11 In its motion, NSTC pointed out that the Court has finally adjudicated and disposed of all
 12 of the claims against the Settling Defendants. NSTC's Brf. at 8. Plaintiffs acknowledge that their
 13 claims against NSTC are distinct from those against the Settling Defendants, but assert that the
 14 remaining and dismissed claims overlap factually. Opp. at 9:16-17. And as the Settling Parties
 15 concede, there are no claims pending against the Settling Defendants. Entry of final judgment
 16 under Rule 54(b) for a party no longer subject to any claims in a lawsuit is proper. *Continental*
Airlines, Inc., 819 F.2d at 1525; *Alcan Aluminum Corp.*, 689 F.2d at 817.

17 The Settling Parties also have acknowledged that the legal issues remaining in the case are
 18 distinct from those that have been adjudicated. Opp. at 9:16-17. The claims that have been
 19 dismissed from the case focused on the liability of the Settling Defendants, including the Moore
 20 Trust Defendants' liability for breaching their fiduciary duties in the 1998 and 1999 transactions.
 21 As the Court has previously held, the remaining claims focus exclusively on the liability of NSTC
 22 as the successor fiduciary to Mr. Moore.⁵ Because the legal issues that have been decided are

23 ⁵ The Court has held that Plaintiffs' claims against NSTC do not attempt to hold NSTC
 24 vicariously liable for the acts of the Settling Defendants but rather focus on NSTC's own alleged
 25 acts or omissions. *See* Order Denying North Star's Motion for Summary Judgment, 12:7-13;
 26 17:25-18:3 [Dkt. No. 237]. As the Court stated in its Order Denying NSTC's Motion for
 27 Summary Judgment, "Plaintiffs are not directly challenging the 1998 and 1999 transactions
 28 through their claims against North Star; they are challenging North Star's failure to remedy
 breaches made by other fiduciaries in connection with the 1998 and 1999 transaction. This
 failure, which is independently actionable under 29 U.S.C. § 1105(a)(3) [sic], took place long
 after the dates of the transactions themselves." Order Denying North Star's Motion for Summary
 Judgment, 17:25-18:3 [Dkt. No. 237] (emphasis in original).

1 distinct from those that remain to be decided, an appeal filed before the ultimate resolution of this
 2 case would necessarily address different legal issues than a later appeal. The Settling Parties have
 3 simply failed to identify any legal issues that will have to be considered more than once if the
 4 Court enters judgment for the Settling Defendants.

5 The same is true of factual issues. In support of their argument, the Settling Parties note
 6 that they must prove that the Moore Trust Defendants were overpaid for their shares in the
 7 company in order to establish that NSTC breached its fiduciary duty. Opp. at 9:17-19. As this
 8 issue has not yet been decided, however, it would not be the subject of any appeal NSTC might
 9 bring after the Court enters final judgment for the Settling Defendants. The Ninth Circuit,
 10 therefore, would not have to consider this factual issue more than once.⁶

11 **B. The Settling Parties Present No Just Reason for Delaying Entry of Judgment**
 12 **in Favor of the Settling Defendants**

13 The Settling Parties argue that the Court should delay entry of final judgment for the
 14 Settling Defendants because a decision favoring NSTC would moot the need for an appeal. This
 15 argument ignores that NSTC's claim for indemnity from K-M Industries Holding Co. ("KMH")
 16 relates to attorneys' fees that NSTC did (and continues to) incur. As the legal fees incurred do
 17 not disappear even if the Court enters judgment in NSTC's favor, nothing about the
 18 indemnification dispute becomes moot in the event of a favorable resolution for NSTC.

19 Without citation to any authority, the Settling Parties also contend that because NSTC has
 20 insurance coverage, it has little interest in enforcing the indemnification agreement with KMH.
 21 Opp. at 10:13-20. This argument fails to recognize the wasting nature of the insurance policies at
 22 issue, in which policy limits are reduced by legal fees expended. Every dollar spent on legal fees
 23 reduces the amount available for disposition of the case. In addition, the Settling Parties'
 24 argument ignores that insurance companies set rates based on claims history, causing NSTC
 25 potentially to sustain future insurance premium increases commensurate with policy

26 ⁶ The Settling Parties have not cited a single case holding that it is improper to enter final
 27 judgment for a dismissed party in a case where the remaining issues are legally distinct from the
 28 decided issue, but there may be some factual overlap between the remaining and decided claims.
 NSTC is aware of no such case.

1 disbursements. NSTC's interests in having KMH indemnify it for ongoing legal fees are very
2 real.

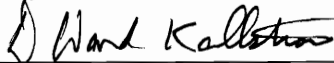
3 For these reasons, the Settling Parties have failed to show that there is any reason, let
4 alone a just reason, to delay the entry of final judgment in favor of the Settling Defendants. The
5 Court should enter judgment for the Settling Defendants.

6 **IV. CONCLUSION**

7 For the reasons discussed above, NSTC respectfully requests that the Court grant it leave
8 to file a motion for reconsideration of its Order Denying North Star's Motion for Judgment on the
9 Pleadings and Granting the Settling Parties' Cross-Motion for Judgment on the Pleadings on the
10 sole issue of the enforceability of Sections 2(b) of the Stock Purchase Agreements. In the
11 alternative, NSTC respectfully requests that the Court enter final judgment as to all claims
12 asserted against KMH and the Moore Trust Defendants.

13 DATED: October 8, 2009

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Company

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